https://www.wsj.com/articles/leveraged-etf-seller-urges-investors-to-fight-proposed-regulation-11580390914

ETFS

Leveraged-ETF Seller Urges Investors to Fight Proposed Regulation

SEC says rules would add safeguards around selling a controversial type of exchange-traded fund

ProShares Chairman Michael Sapir at his office in 2013. **PHOTO:** MARVIN JOSEPH/THE WASHINGTON POST/GETTY IMAGES

By Justin Baer and Paul Kiernan

Jan. 30, 2020 8:28 am ET

A U.S. securities regulatory proposal threatens to shake up the market for exchange-traded funds that draw on derivatives to amplify returns, and a top seller of those funds is urging its investors to push back.

The Securities and Exchange Commission unveiled rules in late 2019 that would require brokers and advisers to pose a series of questions to their clients before they could sell them leveraged ETFs. The clients' responses, the SEC has said, would help advisers determine whether investors understood the risks that accompany funds.

> Michael Sapir, chairman of ETF manager ProShares, said the proposed rule could lead more advisers to stop selling leveraged ETFs altogether.

"We think it's bad for investors," he said. ProShares, a $40 billion money manager that specializes in leveraged funds, prompted its investors to write the SEC voicing their displeasure with the proposal.

The SEC's changes, if adopted, would be an unusual step. While regulators limit the sale of many riskier, private or illiquid investments to qualified investors, publicly traded securities and funds may be bought without those restrictions.

"From our standpoint, this is a bad precedent that breaks with how things have worked since the beginning of securities regulation," Mr. Sapir said.

Leveraged ETFs and mutual funds invest in derivatives that can magnify the returns of a basket of stocks, often tracking an index. The use of derivatives can also multiply potential losses. And while leveraged funds have been around for more than a decade—ProShares said it launched the first in an ETF wrapper in 2006—they remain controversial.

Larry Fink, chief executive of BlackRock Inc., the world's biggest ETF manager, has said leveraged funds were destined to "blow up the whole industry" and questioned why regulators had approved them in the first place. BlackRock doesn't sell any leveraged funds.

SHARE YOUR THOUGHTS

Do you think leveraged exchange-traded funds should be treated differently from other publicly traded securities and funds? Why or why not? Join the conversation below.

Last year, there were 166 leveraged ETFs managing a combined $34.7 billion, according to Morningstar Direct. That was up from 136 funds in 2010 but unchanged from 2015's total.

The SEC's two Republican commissioners issued a statement in November criticizing the proposed rule as one that would "micromanage broker-dealers and advisers" and questioning its necessity.

The two Democratic commissioners argued in their statement on the proposal that some investors may not understand fully leveraged ETFs, particularly in how they perform over longer periods.

"The data show that too many investors buy and hold these products on the expectation that they are sound investments over the long term—when they're usually not," SEC Commissioners Robert Jackson Jr. and Allison Lee wrote.

Many money managers and brokers, though, have yet to weigh in. By Thursday, the proposal had drawn only a handful of comments on the SEC's website. The deadline is March 24.

"It's in effect making it difficult for investors to invest in these products," said Jay Baris, a partner at Shearman & Sterling who represents investment funds, of the SEC's proposal. "Most people are not caring about it because they don't offer leveraged funds."

ProShares is among those that do, and it isn't happy. The Bethesda, Md., firm sent a letter to its investors late Wednesday imploring them to write to the SEC if they believe the funds "are important to you" and "you don't want a third party evaluating your capability to [understand how leveraged funds work] and potentially preventing you from buying them."

Write to Justin Baer at justin.baer@wsj.com and Paul Kiernan at paul.kiernan@wsj.com